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The Director of Central Intelligence
Washington, D.C. 20505

National Intelligence Council

NIC #02925-86
19 June 1986

MEMORANDUM FOR: Director of Central Intelligence
Deputy Director of Central Intelligence

VIA: H. F. Hutchinson, Jr. H
Acting Chairman, National Intelligence Council

FROM: [redacted] 25X1
Acting National Intelligence Office for Economics

SUBJECT: Some Thoughts on a Mexican Debt Moratorium

1. President Garcia's decision to limit Peru's foreign debt payments provides us with some insights as to what we might expect should Mexico undertake some sort of debt moratorium.

-- The savings in foreign interest payments gave Peru sufficient liquidity to conduct foreign trade even as banks rolled back their short-term credit lines; it did not, as some predicted, precipitate a trade crisis.

-- Nearly one year after the debt action the Peruvian economy still seems outwardly to be performing well, certainly better than it would have if Garcia had attempted to implement his populist economic program and continue foreign interest payments.

-- The temporary benefits from the limitation on debt payments will dissipate soon, the result of domestic shortages and the freeze on the level of the inti vis-a-vis the dollar causing import needs to increase. These effects will soon outweigh the savings from the limit on interest payments, resulting in a decline in foreign reserves.

2. Similar short-term benefits will accrue to Mexico should it undertake a moratorium.

-- The country would save around $9 billion per year in annual interest --equivalent to 5 percent of GNP and half of export earnings--roughly the equivalent of a $170 billion annual windfall to the US economy.

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-- The timing of the onset of negative effects of a moratorium would depend on a) the extent to which Mexico maintains the peso at an unrealistically high rate, b) the level of government deficit spending prior to the 1988 Presidential election, and c) to a much lesser extent, possible US actions to minimize or exacerbate the impact of a moratorium. Given the magnitude of the savings, I believe there is room for de la Madrid to keep the economy moving through the remainder of his term. This is not to imply that economic performance will be good; rather, that per capita income may remain flat over the next two years instead of declining by perhaps 10 percent or more under a scenario of minimum bailout with continued payment of foreign interest.

3. If this analysis is correct we must view the no bailout option as a long-term strategy aimed at setting the stage for deterioration beyond 1988 and creating internal political pressures for reconciliation and reform after de la Madrid leaves office. We will have little control over the rate of deterioration except for decisions aimed at keeping political lines open which could undercut to some extent the deleterious effects of a moratorium. (I can envision, for example, decisions not to increase substantially efforts at limiting illegal immigration or drug smuggling on the grounds that these could be seen as political acts of retaliation which could be used to strengthen the hand of the left. Similarly, some may want to encourage Mexico and the banks to isolate from the moratorium short-term credit lines in order to assure continued trade.)

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SUBJECT: Some Thoughts on a Mexican Debt Moratorium

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